

MEMORANDUM

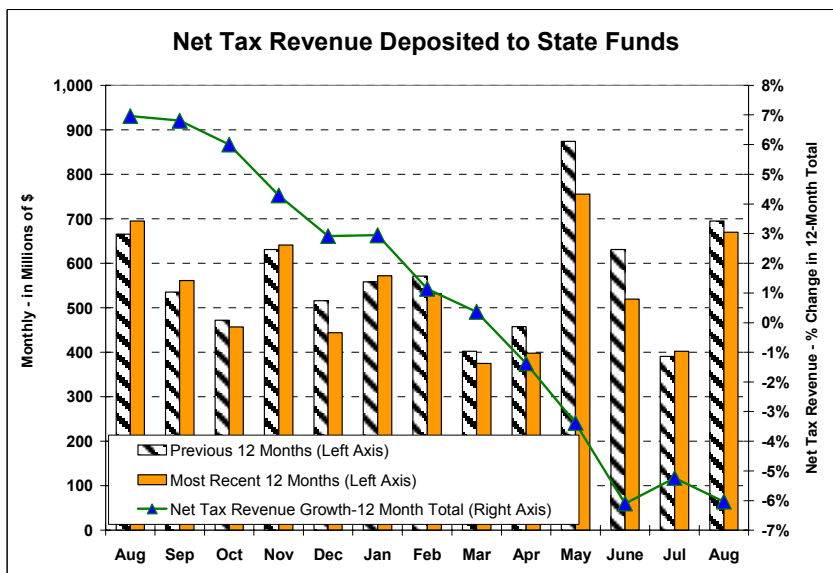
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: September 10, 2009

Twelve-month Total Net Tax Receipts Through August 31, 2009

The attached spreadsheet presents net State tax revenue deposited to State funds for the 12-month period ending August 2009 with comparisons to the previous 12 months. August 2008 to August 2009 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Month of August Comparison

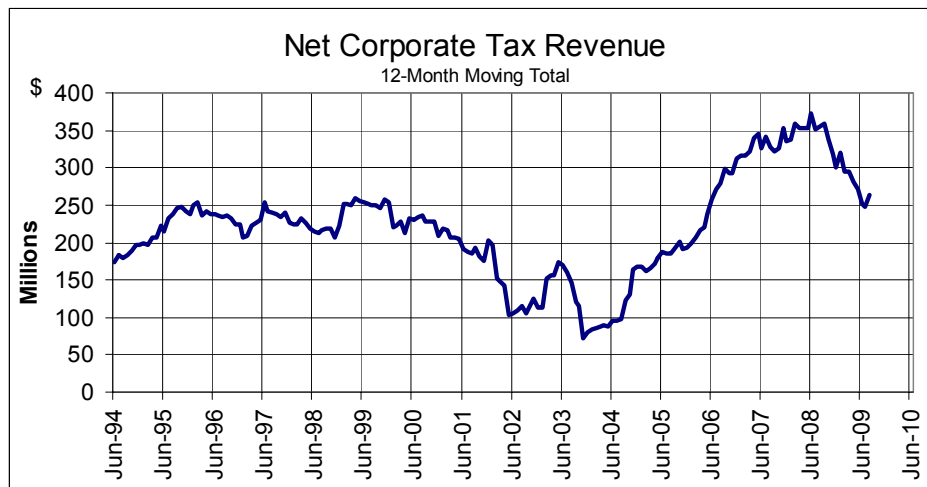
August net tax receipts totaled \$669.2 million, a decrease of \$25.8 million (- 3.7%) compared to August 2008. Major taxes and their contribution to the month's change include:

- Individual Income Tax (positive \$3.5 million, 1.4%) – Gross income tax receipts increased \$1.9 million in August. Withholding payment growth was 1.4% for the month of August. Income tax refunds were \$1.6 million lower for the month.
- Sales/Use Tax (negative \$32.5 million, - 10.7%)
 - Road Use Tax Fund use tax and fees for new registrations decreased \$5.1 million.
 - Gross General Fund sales/use tax receipts decreased \$27.7 million and refunds issued for the month decreased \$0.3 million (net decrease of \$27.4 million). The majority of the decrease is related to the filing of quarterly returns for the April-May-June quarter. Those return payments are deposited in early August.
- Corporate Income Tax (positive \$14.7 million) – Gross receipts increased \$0.7 million and refunds decreased \$14.0 million, the second consecutive month corporate tax refunds declined.
- Fuel Tax (positive \$0.7 million, 2.1%) – Gross fuel tax revenue decreased \$0.4 million while refunds processed in the month decreased \$1.1 million.
- Cigarette & Tobacco Taxes (negative \$0.4 million, - 1.9%) – A \$0.62 per pack federal tax increase, effective April 1, 2009, is providing downward pressure on cigarette sales. The one-year anniversary of Iowa's restrictions on indoor smoking has passed, so monthly percentage drops in cigarette sales should not be as large going forward.
- Gambling Tax (negative \$1.5 million, - 6.2%) – Adjusted gross revenue for Iowa's 17 gambling facilities decreased 8.7% in August 2009, compared to August 2008, and gambling tax revenue growth has now been negative for six consecutive months.

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending August 2009, net revenue from all taxes deposited to State funds totaled \$6.328 billion, a decrease of \$406.7 million (- 6.0%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$173.9 million, - 6.0%) – The rate of individual income tax receipt growth has decreased significantly since peaking in May 2008 at 11.8% year-over-year. The processing of tax year 2008 tax returns during the spring of 2009 accelerated the decrease. Withholding payments to the State increased \$37.4 million over the past 12 months. Of that increase, \$16.3 million was transfers of withholding from unemployment payments and \$10.2 million was transfers from State payroll and retirement funds, with only \$8.6 million in growth for the year from private sector and public sector employees not part of the State accounting system. Over the previous 12 months (ending August 2008), that amount was \$169.5 million.
- Sales/Use Tax (negative \$94.3 million, - 4.2%) – Net sales/use tax receipts have been down eight of the past nine months compared to the same month the previous year and the annual percent growth has fallen from positive 5.6% at the end of August 2008 to negative 4.2% at the end of August 2009.
- Corporate Tax (negative \$92.0 million, - 25.9%) – Net corporate income tax totaled \$263.4 million for the 12 months ending August 2009. The 12-month total peaked in June 2008 at \$371.9 million, so net corporate tax revenue is 29.2% below the latest peak. During and after the 2001 recession, net corporate tax receipts fell 68.8%, peak to trough. The following chart provides an historical depiction of net corporate tax revenue since 1994.



- Fuel Tax (positive \$2.0 million, 0.5%) – Net motor fuel tax revenue has been weak the past twelve months, likely the result of decreased economic activity caused by the recession. According to Department of Revenue fuel sales reports, over the most recent 12-month period Iowa taxable gasoline/ethanol gallons sold increased 0.4% while taxable diesel sales were down 7.9%, the tenth consecutive month showing a decline in annual taxable diesel sales.
- Gambling Tax (negative \$3.3 million, - 1.1%) – Despite expansions of casinos in Clinton and Dubuque, two changes providing boosts to year-over-year gambling growth, gambling tax revenue is modestly negative year-over-year. According to Racing and Gaming Commission statistics, eleven of Iowa's seventeen casino/track locations reported negative annual adjusted gross revenue (AGR) growth for the 12-month period ending August 2009. The AGR growth for all facilities was negative 1.8% over the past 12 months. Excluding the two expanded facilities, growth was negative 4.3%.
- Cigarette and Tobacco Tax (negative \$15.3 million, - 6.1%) – The second anniversary of the State tax increase has passed and the tax increase no longer impacts the year-over-year growth calculation. Iowa's indoor smoking ban and a recent increase in the federal cigarette tax are likely contributors to the tax revenue decline.
- Insurance Premium Tax (negative \$27.3 million, - 25.4%) – The lack of growth in insurance premium tax revenue is the result of expanded use of tax credits, including credits earned through an insurance company's own activities as well as tax credits purchased from others.

Tax Spotlight – Corporate Income Tax

Corporate Income is taxed under the authority of Chapter 422, Division III, Code of Iowa. The tax is imposed on the net income of corporations doing business in Iowa or receiving income from property located in Iowa. Taxation of corporate income by the State of Iowa is based on the share of total company sales occurring within Iowa (single factor formula). Corporate income tax rates are applied as follows:

- Six percent on the first \$25,000 of net income
- Eight percent on the next \$75,000
- Ten percent on the next \$150,000

- Twelve percent on amounts above \$250,000

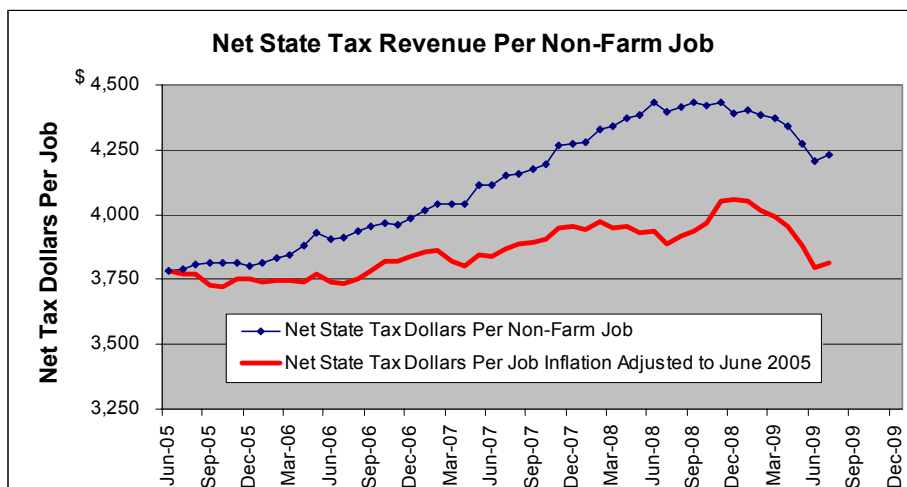
An alternative minimum tax may be imposed at an effective rate of 7.2% if it exceeds the corporation's regular tax liability. Iowa is similar to most states using the federal corporate taxable income of a corporation as the basis for Iowa corporate income tax. Iowa allows for the deduction of 50.0% of federal corporate income tax paid prior to calculating State corporate income tax liability.

The Iowa corporate income tax was first imposed in 1934 at a single rate of 2.0% with the passage of HF 1 (Income, Corporation, and Sales Tax Act). The rate remained at 2.0% until 1955 when it was increased to 3.0%, decreased to 2.0% in 1957, increased again to 3.0% in 1959, and increased to 4.0% in 1965. With the passage of HF 702 in 1967, the corporate income tax rate was changed from a single rate to varying rates at different income levels starting at 4.0% on the first \$25,000, 6.0% on the next \$75,000, and 8.0% for amounts above \$100,000. In 1971, HF 654 increased the rates 2.0 percentage points (6.0%, 8.0%, and 10.0%). The current corporate income tax rates and income levels were approved in HF 2171 (Taxation Act of 1982).

Corporate tax returns are filed by the last day of the fourth month following the end of the corporation's tax year. Cooperatives (as defined by the Internal Revenue Code) are to file a return by the 15th of the ninth month after the end of the cooperative's tax year. Nonprofit corporation returns are due by the 15th of the fifth month after the end of the nonprofit corporation's tax year. Most corporations are required to make estimated tax payments quarterly. All corporate income tax revenues are deposited in the State General Fund.

Tax Revenue and Employment

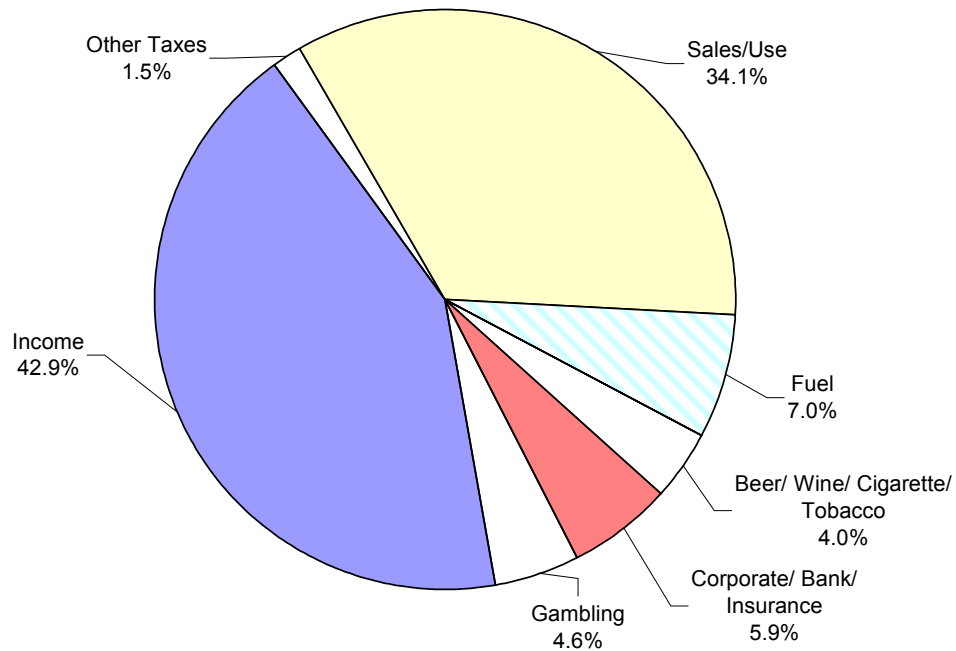
The average reading for Iowa non-farm employment over the 12 months ending July 2009 is 1,502,900, and net State tax receipts over the same 12 months totaled \$6.353 billion, or \$4,227 per non-farm job. This is \$442 (11.7%) higher than the per-job average for July 2005. Over that same time period, inflation (CPI-U) increased 10.7%. Therefore, tax revenue per job has exceeded the rate of inflation since July 2005 by roughly 0.2% per year. The following chart provides an historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



Net State Tax Revenue - Twelve Months Ending August 2009

Net Revenue = \$6.328 Billion

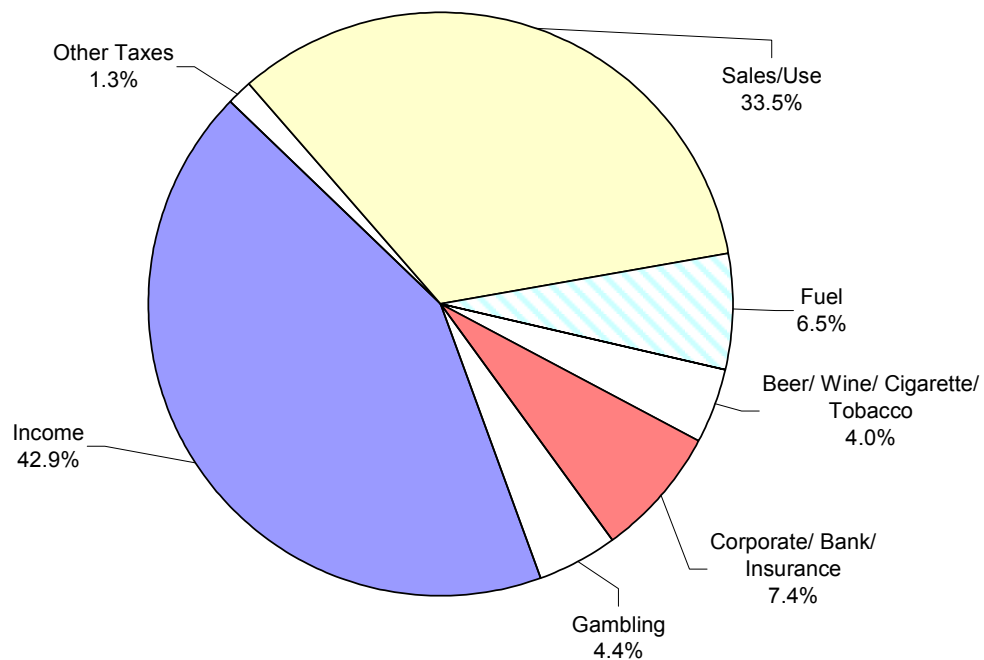
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending August 2008

Net Revenue = \$6.734 Billion

Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of August 2008	Month of August 2009	August \$ Change	August % Change
Banking	\$ 33.7	\$ 28.1	\$ - 5.6	-16.6%	\$ 0.1	\$ 0.1	\$ 0.0	0.0%
Beer & Wine	20.8	21.0	0.2	1.0%	2.0	1.9	- 0.1	-5.0%
Cigarette & Tobacco	250.0	234.7	- 15.3	-6.1%	21.6	21.2	- 0.4	-1.9%
Corporate Income	355.4	263.4	- 92.0	-25.9%	- 0.8	13.9	14.7	--
Fuel	441.1	443.1	2.0	0.5%	33.6	34.3	0.7	2.1%
Gambling	293.6	290.3	- 3.3	-1.1%	24.3	22.8	- 1.5	-6.2%
Individual Income	2,888.5	2,714.6	- 173.9	-6.0%	251.1	254.6	3.5	1.4%
Inheritance	78.9	70.9	- 8.0	-10.1%	8.4	5.7	- 2.7	-32.1%
Insurance	107.6	80.3	- 27.3	-25.4%	46.2	39.0	- 7.2	-15.6%
Other Taxes	- 6.4	7.1	13.5	--	2.3	2.4	0.1	4.3%
Real Estate Transfer	16.9	14.2	- 2.7	-16.0%	1.5	1.1	- 0.4	-26.7%
Sales/Use	2,254.3	2,160.0	- 94.3	-4.2%	304.7	272.2	- 32.5	-10.7%
Total Net Taxes	<u>\$ 6,734.4</u>	<u>\$ 6,327.7</u>	<u>\$ - 406.7</u>	-6.0%	<u>\$ 695.0</u>	<u>\$ 669.2</u>	<u>\$ - 25.8</u>	-3.7%
Gross Tax & Refunds								
Gross Tax	\$ 7,493.0	\$ 7,575.7	\$ 82.7	1.1%	\$ 767.5	\$ 724.8	\$ - 42.7	-5.6%
Tax Refunds	\$ - 758.8	\$ - 1,247.8	\$ - 489.0	64.4%	\$ - 72.6	\$ - 55.4	\$ 17.2	-23.7%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 5,769.9	\$ 5,381.4	\$ - 388.5	-6.7%	\$ 629.8	\$ 609.6	\$ - 20.2	-3.2%
Road Use Tax Fund	\$ 707.1	\$ 697.6	\$ - 9.5	-1.3%	\$ 61.1	\$ 56.7	\$ - 4.4	-7.2%
Non-GF Gambling	\$ 236.1	\$ 230.4	\$ - 5.7	-2.4%	\$ 1.5	\$ 0.9	\$ - 0.6	-40.0%
Other State Funds	\$ 21.2	\$ 18.4	\$ - 2.8	-13.2%	\$ 2.5	\$ 2.3	\$ - 0.2	-8.0%
Local Option Taxes *	\$ 728.2	\$ 805.8	\$ 77.6	10.7%	\$ 60.2	\$ 68.7	\$ 8.5	14.1%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

Tax Categories Used in Table

Franchise (Bank) Tax: Taxes on banks are deposited to the State General Fund. State credit union tax is included on this line also.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

Cigarette & Tobacco Tax: Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

Corporate Income Tax: All corporate tax is deposited to the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: The first \$60.0 million of gambling tax revenue each fiscal year is deposited to the State General Fund. Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, The Gambler's Assistance Fund, the County Endowment Fund, the Endowment for Iowa's Health Account, and the Vision Iowa Fund.

Individual Income Tax: Most individual income tax revenue is deposited to the State General Fund. A total of \$4.0 million per year is deposited to the Workforce Development Fund (\$4.0 million). An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited to the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited to the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited to a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 95.0% to the State General Fund and 5.0% to the Shelter Assistance Fund. The distribution of real estate transfer tax revenue changes beginning FY 2010, when the State General Fund percentage begins a decline to 65.0% by FY 2015.

Sales/Use Tax: General sales/use tax is deposited to the State General Fund, while most vehicle use tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Starting FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.